

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 2010-132-W - ORDER NO. 2011-163

MARCH 1, 2011

IN RE: Application of May River Water Company,)	ORDER APPROVING
Incorporated for Adjustment of Rates and)	ADJUSTMENT IN RATES
Charges)	AND CHARGES
)	

This matter comes before the Public Service Commission of South Carolina (hereinafter the "Commission") on the Application of May River Water Company, Inc. ("May River" or "the Company") for an adjustment to its rates and charges for water services provided to its customers in the May River subdivision in Beaufort County, South Carolina.

May River is a water utility providing water supply and distribution services to 28 residential customers in the May River Plantation subdivision in Beaufort County. The Company provides adequate water supply services to its residential customers using a single deep-drilled well. May River is classified as a NARUC Class C water utility according to the revenue reported on its Application for the test year ending December 31, 2009. May River formerly operated under South Atlantic Utilities, Inc. ("South Atlantic"), which is located in Savannah, Georgia. May River applied to the Commission, and was granted under Order No. 2009-66 in Docket No. 2007-319-W,

approval to transfer South Atlantic's South Carolina customers and water systems to May River.

This matter was initiated on September 8, 2010, when May River filed with this Commission an Application for an adjustment to its rates and charges for the provision of water service. See S.C. Code Ann. §58-5-210 (Supp. 2010). By its Application, the Company sought an increase in annual water revenues. The Company proposed an increase in its current base rates and the implementation of an inclining block rate structure for usage, as well as an increase in availability fees. In its Application, May River requested to increase the base facility charge from the current \$30.00 per month to \$65.00 per month. Additionally, the Company proposed to eliminate the current 10,000 gallons from inclusion in the base facility charge and to initiate a commodity charge of \$4.50 per one thousand gallons for the first 4,000 gallons, a rate of \$5.50 per one thousand gallons for 4,001 to 6,000 gallons, and \$6.50 per one thousand gallons for any water in excess of 6,000 gallons per month. The Company also proposed increasing the current availability fee from \$16.00 per month to \$32.00 per month. May River proposes to continue billing its customers on a bi-monthly basis. Based upon the Company's proposed increases to the base facilities charge, availability fee, and inclining block rates, May River's Application sought additional operating revenues of \$26,401 for a total operating revenue of \$38,185.

By letter dated September 15, 2010, the Commission's 'Clerk's Office instructed May River to publish a prepared Notice of Filing, one time, in newspapers of general circulation in the area affected by the Company's Application. The Notice of Filing

described the nature of the Application and advised all interested persons desiring to participate in the scheduled proceedings of the manner and time in which to file appropriate pleadings for inclusion as a party of record. In the same letter, the Commission also instructed May River to notify directly, by U. S. Mail, each customer affected by the Application by mailing each customer a copy of the Notice of Filing. May River furnished the Commission with an Affidavit of Publication demonstrating that the Notice of Filing had been duly published in a newspaper of general circulation in the area affected by May River's Application. The Company also provided the Commission with a letter in which May River certified that it had complied with the instruction of the Commission's Clerk's Office to mail a copy of the Notice of Filing to all customers affected by the Application.

A Petition to Intervene was filed in this case on October 18, 2010, by Margaret M. Fox, Esquire, of the McNair Law Firm on behalf of the May River Plantation Owners' Association, Inc. ("POA" or "Intervenors") in response to the Notice of Filing. Pursuant to S.C. Code Ann. Section 58-4-10(B) (Supp. 2010), ORS is also a party of record in this proceeding. On December 22, 2010, Ms. Fox withdrew as counsel for the POA and May River subsequently filed a Motion to Dismiss the POA as a party on December 30, 2010. On January 5, 2011, the Commission granted May River's Motion to Dismiss and dismissed the POA as a party to this action on the basis that it was not represented by counsel as required under S.C. Code Ann. Regs. 103-804(T). It was noted in the Commission Directive that customers of the system would still be afforded the

opportunity to testify as public witnesses at the merits hearing on the Application on January 13, 2011.

A public hearing was held before the Commission on January 13, 2011, at the Commission's offices located at 101 Executive Center Drive, Columbia, South Carolina. The Commission, with Chairman John E. "Butch" Howard presiding, heard the matter of May River's Application. May River was represented by Benjamin Mustian, Esquire. ORS was represented by Jeffrey M. Nelson, Esquire. F. David Butler, Esquire, served as legal counsel to the Commission.

Prior to the presentation of the Company's case, the Commission took testimony from public witnesses including Bobby Mendenhall, Misty Monte, Joseph Highsmith and Lee Brewer who are customers of the May River system. The public witnesses asserted that May River should not be entitled to any increase in its rates or charges on the basis that May River could alleviate the need for an increase in rates through a reduction in the costs of operating the May River water system.

May River presented its case in support of the Application through the testimony of Jacquelyn Watson, a Certified Public Accountant and partner in the accounting firm of Watson & Associates, P.A., and Thomas A. Smith, III, Manager of May River. Ms. Watson provided testimony regarding the financial statements of May River, pro forma adjustments, assets and depreciation rates, and revenue calculations under current and proposed rates in the Company's application. Ms. Watson stated that, during the test year, May River experienced a per book net loss of (\$22,897.08) which results in an operating deficit of (194.30%). She also testified that May River experienced an increase

in per book operating expenses of \$24,296 since its last rate case which demonstrates May River's need for rate relief. According to Ms. Watson, the Company is losing money on its operation of the water system and without rate relief, the Company's ability to exist and provide quality services over time will be jeopardized. Based on the proposed rates, Ms. Watson stated that the Company would only have an operating margin of 3.41%, but that the requested rates are just and reasonable when considering the size of the Company. However, Ms. Watson stated that even if the Company's expense items were adjusted such that the Company's resultant operating margin was greater, the Company's expenses incurred would still warrant the rate relief requested. Ms. Watson testified that May River, therefore, believes that its requested rates are necessary to allow the Company to move closer to being on sound financial footing.

Ms. Watson further addressed the relationship between May River and Water Utility Management, LLC ("WUM"). WUM is a separate corporate entity which provides support services to May River and its sister corporations in Georgia. Ms. Watson stated that these services include plant maintenance, repair and construction, meter reading, water testing, compliance of state requirements and the like. Ms. Watson testified that, because WUM provides these services to all of May River's sister companies in Georgia, serving a total of approximately 10,000 customers, this arrangement allows May River to more efficiently provide utility services to its customers in South Carolina at a reasonable cost and to more effectively manage its operational responsibilities. According to Ms. Watson, WUM performed an analysis of its cost to provide these services, and that, in order to determine whether it could secure

services provided by WUM in the open market at a cheaper rate, May River requested estimates from independent third-party vendors to operate and manage the May River system. Based on the Company's investigation, Ms. Watson stated that the amount paid by May River to WUM for management services reflects WUM's costs in providing these services and is comparable to what is available in the open market. Therefore, Ms. Watson testified that the Management Fee charged by WUM to May River is reasonable.

Mr. Smith provided historical background on May River and the operation of the May River water system. He stated that the May River system was constructed in 1973 and that, in the two years since the Commission last granted a rate increase, May River had experienced increased operational expenses for purchased power, labor, taxes and assessments. Further, the Company had made improvements to the system including the installation of a new fence, backflow preventers at each residence, and an hour meter on the system's well pump. Mr. Smith summarized the proposed increase in rates and charges, and stated that the change to usage "tiers" for consumption would encourage water conservation by May River's customers.

Mr. Smith further testified regarding the Management Fee charged by WUM. WUM is a sister company of May River and provides water system operational services to May River and its other sister companies which are located in Georgia. Because May River is the only sister company which operates in South Carolina, May River is subject to significantly different regulatory and accounting requirements. In order to accurately capture WUM's costs to provide operational services and due to the small customer base of May River, Mr. Smith testified that WUM charges May River a monthly service

charge, known as the Management Fee, which reflects WUM's price to provide these services. Additionally, Mr. Smith testified that May River requested and received quotes from other providers who provide water operation services similar to those provided by WUM. Mr. Smith stated that the quotes demonstrate that the price May River pays for these services is equivalent to what is available in the open marketplace and reflects a price which would be obtained at arms-length.

ORS witness Henry Webster testified regarding ORS's examination of the Company's Application. Mr. Webster stated that ORS determined the actual historical costs incurred by WUM in providing services to May River pursuant to the operating services agreement between the two entities. He stated that ORS's examination consisted of verifying May River's operating expenses per the Company's Application, and testing the underlying transactions to ensure that they were properly supported, had a stated business purpose, and were allowable for ratemaking purposes. Mr. Webster further testified that the examination consisted of making adjustments, as necessary, to revenues, expenditures and capital investments, to normalize the test year, using ORS's normal procedures and sampling methods. As a result, ORS ascertained the actual costs of providing service in order to determine an appropriate and reasonable amount of expense for inclusion in rates, rather than the Management Fee as included in the Company's Application. As specified in Mr. Webster's exhibits (Hearing Exhibit 5), after ORS's proposed accounting and pro forma adjustments, May River's total operating expenses for the test year 2009 were reduced from \$34,682 to \$24,063, and its net operating loss was decreased from (\$22,898) to (\$11,598). Mr. Webster further provided that May

River's current operating deficit was calculated by ORS to be (93.04%). After the Applicant's proposed increase in rates and charges, net operating income would be increased to \$12,128 with a resulting operating margin of 30.83%.

ORS witness Hannah Majewski testified regarding ORS staff findings relative to its review of May River's Rate Application. She specifically provided information on ORS's audit of the May River water system, test-year revenues, proposed revenue adjustments and performance bond requirements. Ms. Majewski stated that May River is meeting safe drinking water standards according to recent DHEC sanitary surveys, that DHEC rated the water system as "Satisfactory" during the last sanitary survey, and that May River has a current performance bond on file with the Commission in the amount of \$100,000. Ms. Majewski testified that ORS supported an operating margin for May River of between 10% and 15%.

In his rebuttal testimony, Company witness Smith testified that May River accepted all of the revenue and accounting adjustments testified to by ORS witnesses Webster and Majewski. Further, Company witness Watson testified that May River believed that rates calculated based on ORS's accounting and pro forma adjustments and allowing for a 15% operating margin, were acceptable.

The Commission appreciated the articulate and informative testimony presented by the public witnesses at the hearing. However, in response to the public testimony of the May River customers, who asserted that local, lower cost service providers could lower May River's expenses, Mr. Smith also testified that the estimates submitted by the customers did not include certain necessary costs. Specifically, Mr. Smith noted that the

estimates did not accurately reflect the costs of maintaining the water system. Additionally, Mr. Smith noted that May River's customers failed to take into account recognized costs, including accounting, legal, tax, and regulatory expenses such as those incurred in complying with reporting, record maintenance, accounting requirements, as well as costs relative to maintaining a performance bond which May River must incur as a regulated South Carolina public utility. Moreover, Mr. Smith noted that one of the estimates submitted was obtained from a May River customer and that the customer was, therefore, inclined to submit a reduced rate which may not be available in the open marketplace.

In considering the Application of May River, the Commission must take into account competing interests; the interests of the customers of the system to receive quality service and a quality product at a fair rate, as well as the interest of the Company to have the opportunity to earn a fair operating margin. The Commission must give due consideration to May River's total revenue requirements, including all allowable operating costs. To accomplish this, the Commission must review evidence admitted into the record regarding the operating revenues and operating expenses of May River, and determine adequate and reasonable levels of revenues and expenses for the Company. If the record establishes that a rate increase is warranted for the Company, the Commission will set rates which are just, reasonable, and free from undue discrimination.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

After thorough consideration of the entire record in the May River hearing, including the previously cited testimony and exhibits and the applicable law, the Commission hereby makes the following findings of fact and conclusions of law:

1. May River is a corporation organized and existing under the laws of the State of Georgia and authorized to do business in South Carolina.
2. May River is a public utility as defined by S.C. Code Ann. §58-5-10(3) (Supp. 2010) and provides water service to the public for compensation in the May River Plantation area of Beaufort County, South Carolina and is subject to the jurisdiction of this Commission.
3. May River's current rates and charges for water service and availability fees were approved by the Commission in Order No. 2008-92 in Docket No. 2007-319-W.
4. The appropriate test year period for purposes of this proceeding is the twelve-month period ending December 31, 2009. The test year is contained in May River's Application as well as the testimony and exhibits of the parties' witnesses in this case. The establishment of a test year is a fundamental principle of the ratemaking process. Heater of Seabrook v. S.C. Pub. Serv. Comm'n, 324 S.C. 56, 478 S.E. 2d 826 (1996). The establishment of a test year is used to calculate a utility's expenses and revenues for purposes of determining the reasonableness of a rate. The test year is established to provide a basis for making the most accurate forecast of the utility's rate base, revenues, and expenses in the near future when the prescribed rates are in effect.

Porter v. S.C. Pub. Serv. Comm'n, 328 S.C. 222, 493 S.E.2d 92 (1997). It also provides the Commission with a basis for determining prospective revenue requirements. In the present case, the Commission has concluded that the appropriate test year is the twelve-month period ending December 31, 2009. No party contested the use of this test year as proposed by May River in its Application.

5. In accordance with the Application filed in this case, the Commission will use the operating margin methodology in determining the reasonableness of May River's proposed rates. The Public Service Commission has wide latitude in determining an appropriate rate-setting methodology. Heater of Seabrook, 324 S.C. at 64, 478 S.E.2d at 830 (1996).

6. By its Application, May River requested an increase in rates and charges of \$26,401 to produce an increase in net operating income of \$24,199 after the proposed increase (Schedule B of Exhibit B to Application). By the use of accounting and pro forma adjustments, ORS computed May River's Net Income for Return after the requested increase to be \$12,128 (total operating revenues of \$39,336 less operating expenses of \$27,208). Both May River and ORS calculations of the proposed increase were based on the Proposed Schedule of Rates and Charges contained in Exhibit A to the Company's Application.

7. Total Operating Revenues for May River for the test year per the Company's Application were reported as \$11,784. We accept ORS's calculation of May River's test year total operating revenues, after accounting and pro forma adjustments, as \$12,465. At May River's proposed rates, revenues, as adjusted, were calculated by ORS

to total \$39,336. ORS used consumption data provided by May River and verified during ORS's examination as a basis for its revenue calculations. We find the method of such calculations to be reasonable and fair and therefore accept the above stated service revenue for the test year based upon May River's proposed rates, as adjusted per ORS, to be \$39,336.

8. Operating margins (deficits) for the Company were calculated by ORS Witness Webster, after recommended accounting and pro forma adjustments, to be (93.04%) for the test year and 30.83% after the Company's proposed increase. We approve ORS's adjustments and find May River's per books operating deficit, after accounting and pro forma adjustments, to be (93.04%) for the test year ended December 31, 2009.

9. ORS calculated May River's test year service revenue for metered sales, as adjusted, at \$12,081 and unmetered sales revenues of \$384. Revenues were calculated by ORS for the test year, as adjusted, at \$12,465. See Exhibit HNW-1, Hearing Exhibit 5.

10. The Commission finds that the operating expenses for May River for the test year under present rates and after the appropriate accounting and pro forma adjustments are \$24,063. ORS Witness Webster offered testimony and exhibits detailing the ORS accounting and pro forma adjustments. See, Exhibits HNW-1 through HNW-4, Hearing Exhibit 5. Witness Webster's Surrebuttal testimony addressed ORS's review of May River's Management Agreement with Water Utility Management, LLC and ORS's efforts to determine actual historical costs incurred by WUM in providing services to

May River under that Agreement. The Commission finds that ORS's adjustments to reflect WUM's actual direct and indirect costs in providing service are reasonable. Additionally, the Commission finds that the expenses incurred by WUM in providing services to May River reflect WUM's actual costs in providing such services. Furthermore, the Commission finds that these costs are reasonable based upon the evidence of record, which reflects that the cost for these services is comparable to what is available in the open marketplace. With respect to the testimony of the public witnesses regarding the cost of operating the May River system, the estimates presented did not fully reflect the necessary regulatory, administrative, and operational costs incurred in operating a regulated water system and therefore cannot be considered by the Commission for ratemaking purposes. The revenue impact analysis was performed by ORS and testified to by ORS Witness Majewski and was adopted by Witness Webster in his calculations. Details of the revenue calculations are shown on the Exhibits HKM-2 and HKM-4, Hearing Exhibit 4. Rate case expenses included in the net income for return were those received by ORS as of December 3, 2010.

11. ORS Witness Webster's testimony referred to his Exhibit HNW-2 – "Explanation of Accounting and Pro Forma Adjustments," Hearing Exhibit 5. The witness explained in detail the twelve (12) adjustments proposed by ORS.

12. The Commission finds the accounting and pro forma adjustments proposed by the ORS witnesses Webster and Majewski, as set forth in each witness's direct testimony and supported by the Company's witness Smith, are appropriate for ratemaking purposes. See Hearing Exhibits 4 and 5.

13. The Commission finds that Mr. Webster's Exhibit HNW-3, Hearing Exhibit 5, shows the appropriate depreciation expenses for rate making purposes of \$212. Exhibit HNW-4, Hearing Exhibit 5, shows the accurate computation of the income tax adjustment. All twelve of the ORS proposed adjustments were accepted by May River through the Rebuttal testimony of Witness Watson and from the witness stand by May River witness Smith.

14. The Commission finds that, by accepting all the adjustments as proposed by witnesses Webster and Majewski, the Company's current operating deficit is (93.04%) under May River's presently approved rates and charges. Therefore, the Commission finds that an adjustment of May River's rates and charges is warranted. An increase in rates and charges appears justified for the Company to provide its customers with safe and adequate water service.

15. Based on the operating deficit for the test year contained in Exhibit HNW-1, Hearing Exhibit 5, we find that May River has demonstrated the need for an increase in rates.

16. When applied to the as adjusted test year operations, the rates requested in the Company's Application result in an Operating Margin of 30.83%.

17. The Commission finds that, based on the testimony of ORS Witness Majewski, an Operating Margin of between 10% and 15% is reasonable for a water utility. The Commission further finds that, based on the size and age of the May River system, and considering the impact of the required rate increase upon the customer, an

operating margin of 10% would be appropriate in the circumstances, and would provide a reasonable return to the Company.

18. In order for May River to have the opportunity to achieve an Operating Margin of 10%, the total revenue requirement for May River, using the adjusted operating revenues and operating expenses approved herein, is \$27,629.

19. In order for May River to have the opportunity to earn the herein approved Operating Margin of 10%, May River must be allowed additional annual water service revenues of \$15,164. As part of this increase, the Company is directed to post exterior signage or otherwise mark its business address as the location of the May River Water Company offices.

20. To achieve additional operating revenues of \$15,164, the rates and fees as set forth in Appendix A attached hereto are approved and found to be just and reasonable.

21. The appropriate operating margin for May River based upon the herein approved adjustments and rates is 10%.

22. May River shall maintain records sufficient to ascertain WUM's allocated, direct, and indirect costs incurred in providing services to operate the May River water system.

23. Based on the operating revenues, income, and expenses established through the testimony and exhibits of the parties' witnesses, as well as the small size and age of the May River system, an allowable operating margin for the Company is 10%. See S.C. Code Ann. § 58-5-240(H). An operating margin of 10% provides a prudent

balance between the consumers' need for affordable, quality service and May River's financial health.

IT IS THEREFORE ORDERED THAT:

1. The Schedule of Rates and Charges attached hereto as Appendix A are both just and reasonable and will allow the Company to provide its customers with adequate water services.
2. The Schedule of Rates and Charges attached hereto is approved for service rendered thirty (30) days after the issuance of this Order.
3. An operating margin of 10% is approved for May River.
4. May River shall file all necessary documents, reports and other instruments as required by applicable South Carolina statutes and regulations for the operation of the water system servicing the May River Plantation neighborhood.
5. May River shall keep its books and records according to the NARUC Uniform System of Accounts.
6. May River shall continue to maintain with the Commission and provide a copy to ORS a bond that satisfies the criteria as set forth in S.C. Code Ann. § 58-5-720 (Supp. 2010). The amount of May River's performance bond for water service is \$100,000.
7. May River shall post exterior signage or otherwise mark its business address as the location of the May River Water Company offices.

8. May River shall maintain records sufficient to ascertain WUM's allocated, direct, and indirect costs incurred in providing services to operate the May River water system.

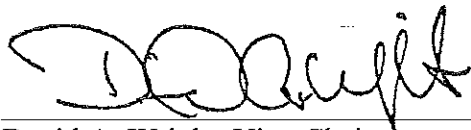
9. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:



John E. Howard, Chairman

ATTEST:



David A. Wright, Vice-Chairman

(SEAL)

Appendix A
Docket No. 2010-132-W
Order No. 2011-163
March 1, 2011

May River Water Company, Inc.

Docket No. 2010-132-W

Schedule of Rates and Charges

MONTHLY CHARGES

METERED WATER CUSTOMERS:

BASE RATE \$30.30 PER MONTH

MONTHLY COMMODITY CHARGES:

\$4.50 PER 1,000 GALLONS	0-4,000 GALLONS
\$5.50 PER 1,000 GALLONS	4,001-6,000 GALLONS
\$6.50 PER 1,000 GALLONS	OVER 6,000 GALLONS

WATER AVAILABILITY CUSTOMERS:

BASE RATE \$30.00 PER MONTH AVAILABILITY ONLY

Customers will be billed once every two months.